

Kentucky Agricultural Finance Corporation

Minutes of the June Meeting

The meeting of the Kentucky Agricultural Finance Corporation was held on June 6, 2005 at 10:00 AM EDT at the Capitol Annex in Frankfort, Kentucky. Mark Farrow, designee for Commissioner Farmer called the meeting to order. Mr. Farrow then asked Lucinda T. Pease, the Secretary to call roll.

Members Present

Mark Farrow, designee for Commissioner Farmer; Wayne Hunt; Jane Jones; Doug Lawson; Bob Proffitt; Kristen Webb, designee for Secretary Robbie Rudolph; Annette Crawford Walters

Members Absent

Harold Benson; Billy Hurd; Billy Joe Miles; Charles Miller; Sandy Ross

Others Present

Staff-Catherine Ball, David Bratcher, Tim Hughes, Lucinda T. Pease, Nicole Ray, Keith L. Rogers

Guests-Brent Lackey, KPAA; Larry Snell, KCCD; Jonathan Thompson, OSBM; Randy Marcum, Cumberland Farm Products; Lowell Atchely, LRC, Karl Frazier, LRC

Notification of Media

Keith Rogers, Executive Director, verified that the media had been notified.

Approval of Minutes

A motion to approve the minutes was made by Wayne Hunt and seconded by Doug Lawson. The motion passed without dissent

Executive Directors Report

Keith Rogers provided the Executive Director's Report.

The next meeting of the KAFC is scheduled for August 5, 2005.

Meeting dates and deadlines for applications will be set and published in the next few weeks. Staff anticipates setting the deadline for applications at two weeks prior to the board meetings.

Mr. Rogers announced a staffing change in the office. Lucinda T. Pease will be leaving the Governor's Office of Agricultural Policy as of June 30, 2005. She will be joining Farm Credit Services in the Lexington, Kentucky office.

Old Business

Tim Hughes informed the board that the application AF05-0005 Joe Moore for a sausage processing facility that was presented at the last meeting has been withdrawn.

New Business

The Alltech loan is still being included in the available balance because they verbally indicated that they would not use the loan proceeds, but we have not received a written withdrawal letter.

The balance also reflects the loan for Mr. Kinslow, which was approved last month.

The Link Deposit program has really picked up now that interest rates have increased.

Loan Applications

PRODUCER ACCELERATED PAYMENT PROGRAM (PAPP)

Keith noted that there is a problem in operating with the third party as originally intended. KAFC had intended to disburse all funds to the Kentucky Produce and Aquaculture Alliance (KPAA) and have all Account Receivable directly collected by KPAA. Several issues were discovered with this approach. Because Brent Lackey is the only employee of KPAA the cost of bonding is \$3,500.00, which is more than they would be getting for administering the program.

There is a flow chart included in the packet, which details how the funds will flow between the administrator, KAFC and the co-op. (On-file with Board Secretary)

Ms. Walters asked for clarification as to who the third party administrator is.

Keith stated that it would be Brent Lackey with KPAA.

Keith reviewed the Producer Accelerated Payment Program (PAPP) request and payment structure. (On file with Board Secretary)

The co-ops have a weekly pool period and all sales delivered are based upon a pool period. Advances from KAFC and payments to KAFC from the co-ops are based on that pool period. The pool period will be closed once all producers are paid and the account receivables are collected and appropriately disbursed. Each pool period will be accounted for separately. KAFC will never advance more than 75% of the value of the approved account receivable nor more than the amount directly advanced to the producers.

In some cases you will find out that we are taking additional securities to back up the accounts receivable.

Mr. Hunt asked which staff personnel will handle the requests.

Mr. Rogers responded that Joel and Bill would handle the money. The requests will go to Bill and he will confer with Joel and Tim and together they will review and authorize payment to be issued. Once we are into the third or fourth pool period, money will be coming back in and they could possibly run through \$700,000.00 dollars with a \$300,000 loan because of the structure. Funds can be transferred between accounts with authorization of both the designated co-op representative and Brent Lackey, KPAA, but any checks have to be signed by the co-op manager and Brent Lackey.

Mr. Bratcher reminded the board that the payment back to KAFC is strictly principle and the interest payment will not be due until the end of the year.

Tim Hughes presented Green River Marketing Produce (GRMP) Application #AF05-0008. The GRMP request is for \$300,000.00 at 2% interest. The security on the loan is

the 1st lien on accounts receivable from customers purchasing agricultural commodities. The advance would be 50% of net returns. Their commodities are cabbage, cantaloupe and watermelon with marketing seasons of June 20/July 1, July 1/August 15 and July 15/August 30, respectively. Based on approval we would be in a subordinate position to KADB. Because the first disbursement of the credit line will occur before the July KADB meeting, KAFC will initially record its lien subordinate to KADB. We will request KADB to subordinate its position to KAFC.

Mr. Hughes commented that the financial info for all of the co-ops is rather bleak, but because the loan is based on accounts receivable we felt it was okay to proceed.

Mr. Lawson noted that GRMP are only list total liabilities of \$1.74, so why are we not taking a blanket lien on assets. We would be foolish not to do this and I recommend we consider this.

A motion to approve the GRPM coop program was made by Annette Crawford Walters and seconded by Doug Lawson with the provision that we take mortgage on any unencumbered assets. The motion passes without dissent.

Tim Hughes presented Cumberland Farm Products (CFP), Application #AF05-0010. The CFP request is for \$125,000.00 at 2% interest. The security on the loan is the first lien on accounts receivables from customers purchasing agricultural commodities. The advance would be no more than 100% of net return to grower. Their commodities are cabbage, tomatoes and pumpkins with marketing seasons of June 15/July 10, July 1/August 15, and September 15/October 15, respectively.

There are no special conditions. Mr. Hughes commented that there are concerns about the 100% request but it is being presented as they have requested. They do have considerable equity as evidenced by recent appraisals on their real estate.

Ms. Walters questioned if the co-op loses if we advance 100%.

Mr. Snell remarked that the co-op was organized in the 1970's in an area of eastern KY where farmers had only enough money to produce the crop but not enough to wait for payment after harvesting. The banks were not initially willing to front the money on bell peppers, etc, all though they are now.

Mr. Rogers noted that the supplied balance sheet only showed the book value of the co-ops real estate and equipment but the recent appraisals were substantially higher.. There is an excess of \$1,000,000.00 in equity that is not showing up. He also noted that the KADB has forgivable loan commitment of \$504,000.

Mr. Lawson questioned the 100% request

Mr. Rogers responded that 100% is the request.

Mr. Lawson asked why we are going to grant 100% for CFP and not GRPM.

Mr. Rogers responded that the co-ops proposed what advance they wanted. If the 75% of advance invoices is reached, we will never go above that. The net return is what farmers eventually end up with.

A motion to accept the CFP request was made by Bob Proffit seconded by Annette Crawford Walters with the mortgage provision on any unclaimed assets. The motion passes without dissent.

Mr. Tim Hughes presented the requests from Central Kentucky Growers Cooperative (CKGC), Application#AF05-0011.

The CKGC request is for \$200,000.00 at 2% interest. The security on the loan is the first lien on accounts receivable from customers purchasing agricultural commodities. The advance would be 75% of net returns. Their commodities are cucumbers, bell peppers and pumpkins with a marketing season of July 1-November 30. Currently the KADB has first lien on accounts receivable. Upon approval KAFC will initially record its lien subordinate to KADB since the first disbursement of the credit line would occur before the KADB's July meeting. At the July KADB meeting, KAFC will request KADB to subordinate its position to KAFC since it will have other collateral securing its forgivable loan.

Ms. Walters asked if the Commonwealth of Kentucky loan from the balance sheet is a loan through KADB.

Mr. Bratcher responded that it is. He also noted that at this time they are the only co-op with repacking revenue throughout the year through their arrangement with Friedas.

Mr. Lawson asked if we know the quality of their receivables

Mr. Snell responded that Frieda's is the customer and Wal-mart is their account and they are reliable.

Mr. Rogers noted that a \$125,000.00 grant for CKGC was just awarded by the KADB and the line of credit will be paid off with a portion of the grant.

A motion to accept the CKGC request with the provision to take mortgage on any unclaimed assets was made by Annette Crawford Walters and seconded by Bob Proffitt. The motion passes without dissent.

Mr. Tim Hughes presented West Kentucky Grower Cooperative (WKGC), application #AF05-0014. The WKGC request is for \$287,000.00 at 2% interest. The security on the loan is the first lien on accounts receivable from customers purchasing sweet corn (if invoices include other commodities in addition to sweet corn, those commodities will also be subject to the lien). The advance would be 75% of grower net return. Their commodities include only the sweet corn and the season runs from May through December. Any existing liens on accounts receivable must be released or subordinated to KAFC lien prior to disbursement of funds.

Mr. Hughes commented that according to their application, Independence bank and KADB are listed as having liens on accounts receivables. Any mortgage on other assets would be the 3rd mortgage behind the bank and the KADB. All of the financials are on hand if anyone wants to view.

Mr. Bratcher noted that they do have debt but their sales have been through Pioneer..

Mr. Lackey noted that they are no longer tied to Pioneer on the sweet corn this year and have 375 acres planted.

Mr. Snell also noted that they have 850 acres of total produce under contract this year.

Mr. Lackey also added that their acreage had doubled since the production manager was hired.

Mr. Hughes reminded the board to keep in mind that we would have to ensure we could get the 1st lien on the accounts receivable.

The motion to accept the WKGC request was made by Wayne Hunt and seconded by Bob Proffitt with the contingency on 1st lien on accounts receivable for sweet corn only along with the subordinate mortgages on real estate.

The motion passes without dissent.

Other Business

Mr. Rogers presented a proposal from Cumberland Farm Products. This is a concept and/or idea that needs feedback from the board. GOAP staff met with CFP last week and learned that Branscum Produce has approached CFP about purchasing Branscum Produce. The new co-op manager, Randy Marcum has extensive experience in the produce industry.

The total purchase price is \$520,000.00. CFP would need a direct loan of \$260,000.00 for the purchase of the business and equipment. They would move the entire operation to the Russell Springs facility. The current Branscum facility would remain with the previous owner. We have seen some cash flow numbers from Branscum and they are positive. We believe this could help CFP become more diverse and seek possible niche markets.

Randy Marcum stated that more volume would open up new markets and opportunities. Being able to centralize the produce will make CFP more available to markets such as Meijers and Wal-Mart. CFP's ability to purchase from smaller farmers along with the Branscum market contacts would be positive. As a whole, KY cannot grow enough produce for the demand, but we need to utilize what we have in the short term and focus on the growing season where KY produce is competitive.

Mr. Bratcher asked if they would be setting up a new entity or continuing as CFP.

Mr. Marcum replied that they would be doing whatever is needed in consideration for CFP's best interest

Mr. Rogers replied that he foresees Branscum ceasing to exist and becoming CFP.

Mr. Marcum responded that the current owner bought the business from his deceased grandfather but he is afraid to go out and invest, whereas he believes CFP can and will be successful at this.

Mr. Rogers asked how old Branscum Produce is.

Mr. Marcum replied that it is approximately 40 years old.

Ms. Walters asked what the total purchase encompasses.

Mr. Marcum replied that the building is only thing we don't get. We get customer base, equipment, etc.

Mr. Rogers replied that the current owner couldn't expand where he is located now.

Another plus is that there could now be an operating facility in Russell Springs.

Mr. Hunt asked where the other \$260,000.00 would be coming from.

Mr. Marcum responded that they anticipate using some other bank loans.

Mr. Hunt asked about the cost of moving the equipment.

Mr. Marcum responded that the move would be relatively easy except for the purchase of new coolers.

Mr. Lawson asked if Mr. Branscum would be signing a non-compete contract.

Mr. Marcum responded that he is agreeing to work with CFP and would be willing to sign.

Mr. Bratcher inquired as to the size of his current customer base

Mr. Marcum responded that the current contract includes prisons, schools and some roadside stands, and he also sells to places in Louisville and Lexington. One of his downfalls is that transportation costs are too high because of low volume loads.

Mr. Bratcher asked if he is making a profit

Mr. Marcum responded yes. He also noted that he has the potential to do \$3,000,000.00 in sales this year

Mr. Hunt asked what the business is worth.

Mr. Marcum responded that he has not seen all the numbers, but believes it is somewhere around \$700,000.00 including the building.

Mr. Hunt asked what the building is worth.

Mr. Marcum responded that he really couldn't accurately say

Mr. Rogers commented that the staff believes this fits within the contract with KADB, but it is new and different from what has been done before. We just want feed back from the board in regards to pursuing this.

Ms. Walters noted that she would certainly recommend that we take a first mortgage on CFP's property if we proceed with the loan..

Mr. Rogers responded that KADB already has the first on the Russell Springs facility.

He also commented that he is excited that this might reopen the Russell Springs facility.

Mr. Hunt commented that he would recommend pursuing this

Mr. Rogers provided two recommendations. Because they want to move forward very quickly, they need to know whether to bring forth an application to the August meeting or let the loan review committee approve a loan for 50 % of purchase price.

Ms. Walters asked how acquiring this business expands CFP's market since Kentucky cannot meet the demand already.

Mr. Marcum responded that CFP may not be handling a lot more produce, but it would allow for year round operation and allow them to do more with the produce. To start out from the ground up would require developing new customer lists, routes, trucks, etc.

Mr. Proffitt commented that he would like to let the loan committee review and make the decision on the loan approval.

Mr. Marcum stated that he would really push the CFP board to go to the bank if we had a quick response and needed immediate action.

Bob Proffitt made the motion and Wayne Hunt seconded the motion authorizing the KAFC Board loan committee to approve a loan to CFP for the purchase of Branscum Produce LLC in an amount not to exceed 50% of the purchase price or a loan in the amount of \$300,000.

An amendment to the motion was made Bob Proffitt and seconded by Wayne Hunt adding Wayne Hunt and Annette Walters to the loan review committee. The amendment passes.

The main motion passed without dissent.

AGRICULTURAL INFRASTRUCTURE LOAN PROGRAM

Mr. Rogers commented that Mr. Hughes has ran into issues on lower loans amounts and the banks not being willing to wait for approval. In response to this we are recommending allowing a GOAP Infrastructure loan review Committee to approve loans

less than \$50,000.00, which meet certain criteria. Members of the committee would be Tim Hughes, David Bratcher, Bill McCloskey and Keith Rogers. This would allow KAFC approval to be given to lenders in a more timely fashion on smaller loans. The recommendation is that loans meet all the predetermined criteria set by the KAFC Board at the May 2005 meeting and meet or exceed the following Trans Union credit score:

For loans greater than \$30,000.00 and less than \$49,999.99 a score of 710;

For loans greater than \$15,000.00 and less than \$29,999.99 a score of 700; and

For loans less than \$14,999.99 a score of 690.

If the application meets or exceeds these minimum requirements, then the committee will review and approve or refer the loan to the KAFC Board. In the event that an application does not meet or exceed these minimum requirements, GOAP staff will bring the entire application to the Board for the Board for a final determination.

Mr. Hunt made the motion and Mr. Lawson seconded to accept the recommendation. The motion passed without dissent.

Mr. Hughes commented that there have been several requests to add fencing as an eligible project to the AILP..

Mr. Hunt commented that the infrastructure program needs to be very broad.

Mr. Rogers noted that the staff would proceed with these types of requests as he sees comfort among the board.

Another concern presented by Mr. Hughes is in regards to loans without bank participation. As long as project is not finished is KAFC willing to do a loan without bank participation? For example, there is no bank participation because the farmer is putting up other 50%.

Mr. Hunt commented that he feels KAFC is becoming more and more of a bank.

Mr. Rogers noted that there is a provision for direct loans but it is at a higher rate and requires other conditions to be met.

Ms. Jones asked what the rate is.

Mr. Hughes replied it is 3.75%

Mr. Hunt remarked that he believes KADB will tell KAFC to stay away from becoming a bank.

Mr. Rogers commented that KAFC can handle a few direct loans and the staff is handling this fine now with KADB

Ms. Jones remarked that KAFC might get more loans through this than anticipated.

Mr. Rogers responded that the biggest labor resource is making the loan

Mr. Hunt responded that he believes the initial thought was that these loans were for when we couldn't get bank participation

Mr. Bratcher asked if this particular applicant has any debt on the property.

Mr. Hunt responded that the first time you do it, you are going to have to keep doing it. I just think it is a bad idea to begin

Mr. Rogers noted that on the other side, part of our job is to take a risk that the bank will not make.

Mr. Hunt replied that the only intention was if a bank could not approve the farmer. Mr. Proffit remarked that the question is, are we using the money to do the right thing for the farmers.

Mr. Hunt replied that the intent was for us to use the money to leverage with the funds provided by the bank.

Mr. Lawson commented that we do a moratorium until Aug 5th

Mr. Rogers remarked that unless the board wants to suspend this until the August meeting we would bring you a clearer message at that time.

Mr. Rogers presented another concern, which is in regards to tobacco dependency. The current guidelines require that you must have a Phase II check, buyout contract or future contract. We have young farmers who have participated in tobacco, but it has never been in their name.

Mr. Hunt responded that we must go back to whether he is a first generation

Mr. Hughes responded that we have two prospects, who have been involved in their family's tobacco production, but don't have receipt of a phase II payment or a buyout or a future production contract.

Mr. Hunt responded that we must be flexible

Ms. Walters questioned if we could get the parent to co-sign.

Mr. Rogers recommended dealing with this on a case-by-case basis and allowing them to plead their case and/or provide a statement. I have no problem letting them provide that and letting us pre-approve initially before they go through the entire application process.

Mr. Hughes also mentioned that lenders had requested that KAFC accept other valuation methods such as a PVA value for property in addition to formal appraisals.

Mr. Rogers commented that all of the AILP requests to be considered at this meeting are for broiler houses in the Murray/Mayfield area.

The first applicant is Greg Smith, Application AF05-0009. The request is for \$100,000.00 at 2% interest for the construction of four poultry houses to be contracted with Pilgrims Pride. The total project cost for buildings and equipment is \$625,000 per application (\$625,716.00 per estimate within application). The security for the loan would be the third mortgage on two farms with an appraised value (discounted to 80%) of \$856,000.00 and the third mortgage on residence with PVA appraisal of \$150,000.00

Tim stated that the lender actually discounted the value of the new poultry houses to 80% of the construction costs..

Staff recommends approval of this loan subject to the execution of the broiler agreement between borrower and Pilgrims Pride.

James Ray Murdock, Applicant AF05-0012, is requesting \$100,000.00 at 2% interest for the construction of two broiler houses to be contracted with Pilgrims Pride. The total project cost for buildings and equipment is \$340,000.00. The security for the loan is second mortgage on 5-acre tract, which will include the two broiler houses, a second lien on all broiler house equipment (included in the construction cost), and a second mortgage

on additional property being offered as collateral. The total of loans ahead of KAFC equals \$766,000.00.

James Ray Murdock is donating a tract of land to his son, Kyle Murdock, the other applicant. James Murdock has two houses, and Kyle Murdock has two houses but each have separate farm numbers

Kyle Murdock, Applicant AF05-0013, is requesting \$100,000.00 at 2% for the construction of two broiler houses to be contracted with Pilgrims Pride. The total project cost for buildings and equipment is \$340,000.00. The security for the loan is second mortgage on 5-acre tract, which will include the two broiler houses and second lien on all broiler house equipment (included in construction cost).

Mr. Hughes noted that Pilgrims Pride predicts a \$95,000 return on a four-house operation James R. Murdock is pledging some additional real estate through construction, but the bank will be releasing the property upon loan closing with our participation.

Mr. Bratcher commented that staff doesn't think there are two different contracts for the Murdock's

Mr. Lawson commented that if it were not individual that would tie us up as to whether we can remain our \$100,000 limit per applicant.

Mr. Hughes remarked that the property will be deeded into Kyle's name and two of the houses are on his property. Both of them meet the tobacco dependency requirements and each property has its own Farm Service Agency Farm Serial Number.

The motion to accept the application for Gregory Smith was made by Doug Lawson and seconded by Annette Walters. The motion passed without dissent.

The motion to accept the application for James Murdock was made by Doug Lawson seconded by Annette Crawford Walters. The motion passed without dissent.

The motion to accept the application for Kyle and Mandy Murdock was made by Annette Walters and seconded by Doug Lawson. This included the home or the father's property as additional collateral. The motion passed without dissent.

YOUNG FARMER LOAN PROGRAM (YF)

Mr. Hughes presented an application for Jeremy Kinslow, Applicant AF05-0015., He is the son of Haskel Don Kinslow who was approved for a KAFC AILP loan last month. The request is for \$60,000.00 at 5.375% interest (based upon Farmer Mac III 20 year fixed rate) for the purchase of (60 acres +/-) which is part of a 100 acre farm proposed to be acquired by his father. The security on the loan would be first mortgage on real estate, with a possible loan guarantee from FSA.

Plans are for the father to purchase property at auction and sell off approximately 60 acres to Jeremy. He should be eligible through FSA but we would not have an appraisal on the property because of the auction scenario.

Sandy Ross, implied that either The Central Bank, USA or South Central Bank would probably do the loan if we are not interested

Mr. Bratcher remarked that KAFC would have to get the guarantee going into the loan.

Mr. Lawson responded that KAFC would need the guarantee up front, because if we agree to fund prior to, it may not be possible to go back and get that security.

Mr. Lawson commented that if FSA approves a direct loan, all we will have to do is attach their application to ours for the guarantee.

It was recommended that the loan has to be in conjunction with FSA and has to have a take out letter from FSA. The loan would be for a \$60,000 maximum loan at \$2,000 per acre and we would have first mortgage.

Mr. Lawson felt that we should leave the rate at the discretion of the loan committee and the market.

The motion to approve the recommendation was made by Doug Lawson and seconded by Wayne Hunt. The motion passed without dissent.

AGRICULTURAL PROCESSING INVESTMENT FUND (APIF)

Agro Ventures Partners of Kentucky, LLC, Applicant AF05-0016 is requesting \$750,000.00 to purchase an 80,000 square foot building in Guthrie, Kentucky to be used to start a business to procure locally produced hay to be processed and sold as quality compressed hay targeted to the equine industry. The security for the loan would be the 80,000.00 square foot Weyerhaeuser building in Guthrie.

Tim noted that KAFC does have the opportunity to purchase the building and lease it to them. At this point it does not show they are putting anything into the project themselves.

Mr. Rogers noted that staff does not particularly like the idea of the request at 100% for the project.

Mr. Hughes also noted that they have been working with Farm Credit Services for over a year and have never gotten approved

The motion was made by Wayne Hunt and seconded by Annette Walters to refer the request to the loan review committee. The motion passes without dissent.

The motion to adjourn was made by Wayne Hunt and seconded by Jane Jones. The motion passes without dissent.

The meeting adjourned at 1:18 PM.